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HOUSE OF REPRESENTATIVES
REPORT
101-303

REVIEW OF CERTAIN ACQUISITIONS OF VOTING SECURITIES OF AIR CARRIERS

OCTOBER 24, 1989.—Committed to the Committee of the Whole House on the State of the Union and ordered to be printed

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Mr. ANDERSON, from the Committee on Public Works and Transportation, submitted the following

REPORT

together with

DISSENTING VIEWS

[To accompany H.R. 3443]

[Including cost estimate of the Congressional Budget Office]

The Committee on Public Works and Transportation, to whom was referred the bill (H.R. 3443) to amend the Federal Aviation Act of 1958 to provide for review of certain acquisitions of voting securities of air carriers, and for other purposes, having considered the same, report favorably thereon with an amendment and recommend that the bill as amended do pass.

The amendment is as follows:

Strike out all after the enacting clause and insert in lieu thereof the following:

SECTION 1. AMENDMENTS TO THE FEDERAL AVIATION ACT OF 1958.

(a) REVIEW PROCESS.—Title IV of the Federal Aviation Act of 1958 (40 U.S.C. App. 1371-1389) is amended by adding at the end thereof the following new section:

"SEC. 420. REVIEW OF CERTAIN ACQUISITIONS OF VOTING SECURITIES OF AIR CARRIERS.

"(a) GENERAL RULE.—No person shall acquire, directly or indirectly, any voting securities of a major air carrier or person who controls a major air carrier unless the acquiring person files notification pursuant to the rules under subsection (d), the waiting period described in subsection (b)(1) has expired, and the Secretary has not disapproved such acquisition under subsection (c)—

"(1) if such acquisition is of 15 percent or more of the voting securities of the acquired person; or

"(2) if, before such acquisition, the acquiring person holds less than 15 percent of the voting securities of the acquired person and, as a result of such acquisi-

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tion, the acquiring person would hold 15 percent or more of the voting securities of the acquired person.

"(b) WAITING PERIOD.—

"(1) GENERAL RULE—The waiting period required under subsection (a) shall—

"(A) begin on the date of receipt by the Secretary of the completed notification required under this section from the acquiring person; and

"(B) end on the 30th day after the date of such receipt or such later date as may be set under subsection (e)(2).

"(2) TERMINATION.—The Secretary may, in individual cases, terminate the waiting period specified in paragraph (1) and allow any person to proceed with any acquisition subject to this section and promptly shall cause to be published in the Federal Register a notice that the Secretary does not intend to take any action within such period with respect to such acquisition.

"(c) DISAPPROVAL.—The Secretary shall disapprove an acquisition of voting securities subject to this section if the Secretary finds—

"(1) that the acquisition is likely to weaken the acquired person financially to such an extent—

"(A) that a deterioration in the ability of the air carrier to comply with its established safety procedures would occur;

"(B) that the air carrier would be unable to take the steps necessary to continue to operate with the highest degree of safety;

"(C) that the air carrier would be required to dispose of a substantial portion of its aviation-related assets in order to meet it financial obligations; or

"(D) that a substantial deterioration in the air carrier's ability to compete in providing air transportation would result;

"(2) that the probable intent to the acquiring person is to make a major reduction in the size of the air carrier by disposing of aviation-related assets; except in any case in which—

"(A) such disposition would be necessary, in the absence of the acquisition, to avoid the financial failure of the air carrier,

"(B) the assets to be disposed of could not be used profitably by the air carrier, or

"(C) such disposition would be in the public interest;

"(3) that the acquisition would result in a person who is not a citizen of the United States having power to exercise control over the air carrier; or

"(4) that the acquiring person is not providing, in a timely manner, the documentary material and information required by the Secretary to make a decision regarding the acquisition under this section.

"(d) FORM OF NOTIFICATION AND OTHER RULES.—

"(1) IN GENERAL.—The Secretary, by regulation—

"(A) shall require that the notification under subsection (a) be in such form and contain such information and documentary material relevant to a proposed acquisition as is necessary to enable the Secretary to determine whether such acquisition should be disapproved under this section, and

"(B) may prescribe such other rules as may be necessary and appropriate to carry out the purposes of this section, including rules relating to the submission by the air carrier of information or documentary material described in subparagraph (A).

"(2) DEADLINE FOR ISSUANCE OF REGULATIONS.—Not later than 10 days after the date of the enactment of this section, the Secretary shall issue regulations necessary to carry out the objectives of this section.

"(e) EXTENSION OF WAITING PERIOD.—

"(1) SUBMISSION OF ADDITIONAL INFORMATION.—The Secretary may, before the expiration of the 30-day waiting period specified in subsection (b)(1), require the submission of additional information or documentary material relevant to the proposed acquisition, from a person required to file notification with respect to such acquisition under subsection (a), from the air carrier, or from any officer, director, partner, agent, or employee of such person.

"(2) DURATION.—The Secretary, in his discretion, may extend the 30-day waiting period specified in subsection (b)(1) for an additional period of not more than 20 days after the later of—

"(A) the date on which the Secretary receives from the acquiring person or any officer, director, partner, agent, or employee of such person all of the information and documentary material required to be submitted pursuant to a request under paragraph (1); or

"(B) the date by which the air carrier or any officer, director, partner, agent, or employee of the air carrier is directed to submit information or documentary material pursuant to a request under paragraph (1).

"(f) PROTECTION OF INFORMATION.—Any information or documentary material filed with the Secretary pursuant to this section shall be exempt from disclosure under section 552 of title 5, United States Code, and no such information or documentary material may be made public, except as may be relevant to any administrative or judicial action or proceeding. Nothing in this section is intended to prevent disclosure to either House of Congress or to any duly authorized committee or subcommittee of Congress.

"(g) COMPUTATION OF VOTING SECURITIES.—For purpose of this section, the amount or percentage of voting securities of a person which are acquired or held by another person shall be determined by aggregating the amount or percentage of such voting securities held or acquired by such other person and each affiliate thereof.

"(h) DEFINITIONS.—As used in this section—

"(1) MAJOR AIR CARRIER.—The term 'major air carrier' means an air carrier with annual revenues of more than $750,000,000.

"(2) VOTING SECURITIES.—The term 'voting securities' means any securities which at present or upon conversion entitle the owner or holder thereof to vote for the election of directors of the issuer or, with respect to unincorporated issuers, persons exercising similar functions.".

(b) CONFORMING AMENDMENT.—The portion of the table of contents contained in the first section of the Federal Aviation Act of 1958 relating to title IV of such Act is amended by adding at the end thereof the following new item:

"Sec. 420. Review of certain acquisitions of voting securities of air carriers.".

PURPOSE OF THE BILL

The reported bill, H.R. 3443, will enhance the powers of the Secretary of Transportation to deal with issues of vital importance to the aviation industry; acquisitions of control of United States airlines involving leveraged buyouts (LBOs) and increased foreign ownership and control. The bill establishes procedures to ensure that there will be a reasonable opportunity for the Department of Transportation to review acquisition proposals before they are completed. The bill also gives the Department authority to disapprove those proposals which would impair an airline's ability to provide safe, reliable and effective service or which would give foreign interests the power to control a United States airline. The bill will not prevent legitimate acquisitions which would not impair the safety or competitive effectiveness of the acquired airline.

CONCERNS ABOUT LEVERAGED BUYOUTS

"Leveraged buyout" is not a precise legal term, but generally describes a recapitalization of an airline in which an acquiring group buys out existing shareholders, funding the acquisition of the airline's stock primarily by having the airline borrow money and take on substantial new debt. The new debt requires the airline to produce a substantial cash flow each year to service the additional debt.

An example of an airline leveraged buyout is the recent acquisition of control of Northwest Airlines by a group headed by Alfred Checchi and Gary Wilson. The acquisition greatly increased the long term debt of Northwest. Before the acquisition, Northwest had long term debt of $385 million; after the acquisition the company's long term debt had increased to $3.1 billion. As a result, Northwest went from a pre-acquisition capital structure in which it had twice as much equity as debt to a post-acquisition capital structure in which equity is 18% and debt 82%. The General Accounting Office

estimated that as a result of the acquisition, the cost of servicing the Northwests's debt would increase from an annual cost of less than $100 million a year, to an annual cost in the $500 million range.

There are increased concerns about the effect of such increases in the long term debt of airlines on the financial strength of the acquired carrier and on its ability to provide safe and effective service. At the aviation Subcommittee's recent hearings on LBO's, the United States Secretary of Transportation testified that "the pressure to pay down the principal and to meet interest payments could threaten the carrier's ability to meet its other obligations including fleet replacement, aircraft repair and maintenence, security, crew training, and other safety-related expenses".

The Secretary had elaborated on these concerns in his remarks to the International Aviation Club on September 19.

> The airline industry is different for a number of reasons:
>
> Number one, the airline industry, even though it's no longer regulated like a public utility, still has public interest responsibilities: Debt-ridden airlines, forced to adopt sweeping austerity measures, may unwittingly threaten the safety of the traveling public. It is my job to ensure that the public responsibility we expect of our airlines are carried out. A few examples:
>
> We are now detecting the extent of aircraft fatigue and corrosion problems. Airlines today cannot afford to scrimp on the new costs of maintaining the safety of their senior aircraft.
>
> We are now discovering the technology to meet the demand for effective noise abatement. Airlines must have the resources to address environmental concerns.
>
> We must do everything possible to fight the despicable acts of terrorism. Airlines cannot afford to cut back on security costs.
>
> * * * * *
>
> Even short of bankruptcy, the high costs of servicing large debt levels may also deny an airline the flexibility to lower fares, expand operations, modernize fleets—in other words, take steps essential to real competition. And given the barriers that appear to be in the way of entry—a subject that we are examining closely—it's not easy to replace a lost competitor. No new major carriers have entered within the last five years.
>
> In short, for these and other reasons, the airline industry stands on a different footing than other industries. This "stall warning" on the part of DOT doesn't signal a return to regulation—I think we can all agree that everyone, especially consumers, have benefited enormously from deregulation. What it signals is that the govenment must remain vigilant in carrying out its remaining oversight responsibilities.

Similarly, Mr. Philip Baggaley, a Vice President, at Standard and Poor's Corporation a debt rating agency, testified before the Aviation Subcommittee that:

> If LBOs continue to spread through the airline industry, the result will be: (1) Greater risk of bankruptcy; (2) Further consolidation; (3) and quite possibly, slower progress on expanding and modernizing the industry's aircraft fleet.
>
> Given the role which airlines play in our national transportation system, and in the economy as a whole, that would affect not only shareholders and creditors, but employees and the entire traveling public.

Mr. Baggaley and other witnesses pointed out that although companies in stable, recession-proof industries can safely support large amounts of debt. Airlines, at least historically, have not been stable or recession proof. For example, during the 10 year period, 1979 through 1988, the financial results of operations by United States scheduled airlines varied widely, as indicated by the following table.

TABLE I.—*Net Profits of U.S. Scheduled Airlines, 1979–88*

[Amounts in parenthesis indicates losses; dollars in millions]

1979	$347
1980	17
1981	(301)
1982	(916)
1983	(188)
1984	825
1985	863
1986	(235)
1987	593
1988	1,706

Source: Air Transport Association.

Our concern over leveraged buyouts is heightened by the recent decline in the number of effective competitors in the industry. Deregulation depends on effective competition to ensure that airline passengers can get good service at low fares. The theory of deregulation is that when a carrier begins to abuse its position by charging excessive fares or providing poor service, another airline (a new carrier or an existing carrier expanding service) will be able to enter the market and compete by offering lower fares or improved service.

In the early years of deregulation, competition increased as a number of new carriers began providing scheduled jet service. The new competitors included former intrastate carriers such as Southwest, Pacific Southwest and Air California, former charter carriers such as Capital and World, and entirely new carriers such as Midway and People Express. In the mid 1980's, there was a significant decline in the number of carriers providing service. Of the 22 major new entrants since deregulation, only four survived; the others either failed, were acquired by other carriers, or changed to commuter service. Since 1985, there have been no new entrants other than the Trump Shuttle. In addition, between 1985 and 1987, the Department of Transportation encouraged and furthered con-

centration in the industry by approving 10 mergers of major carriers.

As a result of the substantial decrease in the number of carriers providing service, the market share of the top 8 carriers in the industry increased from 80 percent of revenue passenger miles in 1978, to more than 90 percent today. The traveling public cannot afford to have one of the remaining major airlines dismantled or seriously disabled as an effective competitor by the burden of servicing excessive debt resulting from a leveraged buyout.

Concerns over Foreign Ownership of United States Airlines

Some of the recent acquisition proposals have involved substantial participation by foreign interests. In the takeover of Northwest by the Checchi group, the total equity investment after the takeover was $705 million. KLM Royal Dutch Airlines held $400 million of this equity and Elders IXL, Ltd., an Australian citizen and investment company, held $80 million. Other provisions in the acquisition agreement provided that KLM and Elders would each have one representative on the twelve person Board of Directors controlling Northwest, that KLM and Northwest intended to enter into cooperative operating agreements, and that KLM would have the right to establish a three-person committee to advise Northwest's management on its financial affairs. The KLM participation in Northwest will be reduced substantially as a result of a consent order between Northwest and the Department of Transportation.

A recent proposal for takeover of United Airlines, which is now being renegotiated, contemplated substantial participation by British Airways.

At the Aviation Subcommittee's hearings, a number of concerns were expressed about foreign ownership of United States airlines.

U.S. airlines have committed aircraft to the Department of Defense for use in a national emergency (the Civil Reserve Air Fleet). Foreign ownership may lessen the willingness of U.S. airlines to participate in CRAF.

Foreign airlines and U.S. airlines often compete. Would a U.S. airline compete effectively against a foreign airline which owned some of its stock?

There may be adverse effects on the U.S. government's ability to negotiate aviation bilaterals with foreign governments whose airlines are partial owners of U.S. airlines. Would the U.S. airline leak information about the U.S. position or negotiating strategy to its foreign owners? Would foreign owners pressure U.S. airlines to influence the U.S. Government to take negotiating positions which would benefit the foreign airline?

Adequacy of Current Authority of the Department of Transportation To Regulate Leveraged Buyouts and Foreign Ownership

In dealing with the Checchi group's acquisition of control of Northwest Airlines, the Department used its authority under the Federal Aviation Act to review the transaction and negotiate a consent order with Northwest. The consent order required KLM to reduce its equity participation in Northwest, to limit its participa-

tion on the Northwest Board of Directors, and to eliminate the Committee of KLM representatives which would advise Northwest. On the question of financial fitness, the Department obtained the agreement of Northwest to file a series of continuing detailed reports which would give the Department timely information about Northwest's financial condition.

The Department's actions in the Northwest case have been cited as indicating that the Department's existing authority is adequate to deal with the problems of leveraged buyouts and foreign ownership. The Committee has reservations about the significance of the Northwest decision as a precedent for future DOT action. In the Northwest case, Northwest and the Department entered into a consent agreement; thus the legal interpretations on which the Department based its actions were unchallenged. In a subsequent contested case involving another airline less cooperative than Northwest, a court may be unwilling to sustain DOT's interpretation of its own statutory authority.

In addition, there were limits to the action which the Department took in the Northwest case. The Department did require a divestiture of some of the foreign equity invested in Northwest. However, on the question of financial fitness, the Department did not find that the debt involved in the transaction was excessive and would leave Northwest unfit.[1] Thus, the Northwest case does not furnish a precedent for the Department concluding that a particular level of debt is excessive and must be reduced to restore a carrier to a fit condition. The Northwest case does not indicate how the Department would go about requiring a carrier to reduce its debt after a deal had been completed.

Turning more specifically to DOT's existing authority to deal with the financial structure of a recapitalized airline is based on section 401(r) of the Federal Aviation Act which imposes a "continuing requirement" that each air carrier holding a certificate to provide air transportation must be "fit, willing and able" to provide this transportation. This authority could be used to prevent or undo a leveraged buyout in a case in which DOT was able to find that after a leveraged buyout was completed the acquired air carrier would no longer be "fit, willing, and able."

We have several reservations about the adequacy of this authority to deal with LBOs. First, section 401(5) does not require a person attempting a takeover to seek prior approval from DOT. Rather, under section 401(r) the burden is on DOT to start a proceeding and find the carrier unfit. This means that an acquisition can be completed before DOT finishes its review. This would place DOT in a difficult position. If an acquisition is completed and the carrier has taken on extensive new debt and used the debt proceeds to buy out existing stock holders, would DOT's only option be to revoke the carrier's certificate? Would there be any practical way for DOT to require that the transaction be unscrambled and the carrier restored to a sound financial condition? Could the prior stockholders be required to pay back to the airline the money they

[1] The Department did require Northwest to file continuing detailed financial reports so that the Department could continue to monitor Northwest's fitness.

had received for their stock, so that the airline would be able to liquidate any excessive debt?

In addition there is uncertainty about the extent of DOT's power to find an airline financially unfit. There are only limited precedents on this issue, since the Department has never found a major airline to be in violation of its duty to continue to be fit. Historically, the fitness authority has been interpreted narrowly. At the Aviation Subcommittee hearing, Michael E. Levine, Dean of the School of Organization and Management at Yale University and a former General Director of the Civil Aeronautics Board, testified that:

> Fitness is an all or nothing "permission to operate" standard which has historically allowed airlines very wide latitude in choosing their capital structures. Declaring an airline unfit to fly is a weapon which should be reserved for situations where an airline endangers the flying public by its inability or unwillingness to do business in a way which would protect the public's money or their lives. When I was at CAB, we summed up the standing asking, "will they steal or will they kill?" If the answer was no, an airline was fit even if it might not make money.

The Department of Transportation, which took over the CAB's authority in 1985 has suggested that the fitness authority is more broadly based and covers cases in which an airline would be able to fly safety, but impaired in its ability to provide effective or reliable service. However, there are no DOT or court precedents establishing clear standards for interpreting "fitness" in situations not involving safety or loss of consumer funds.

In many cases, there would be serious problems with the Department using its fitness authority to find that a leveraged buyout involving a major carrier would leave that carrier unfit. If DOT were to find that a leveraged buyout would leave an airline such as Northwest or United unfit, DOT might be required to challenge the fitness of other airlines such as Pan American, Continental and TWA, since these carriers have an even higher debt-to-equity ratio than Northwest has, or than United apparently would have had under its original acquisition plan.

DOT's authority to regulate foreign ownership of United States airlines is based on the requirement in the Federal Aviation Act that a United States air carrier must be a "citizen of the United States" which is defined as follows:

> (16) "Citizen of the United States" means (a) an individual who is a citizen of the United States or of one of its possessions, or (b) a partnership of which each is such an individual, or (c) a corporation or association created or organized under the laws of the United States, of which the president and two-thirds or more of the board of directors and other managing officers thereof are such individuals and in which at least 75 per centum of the voting interest is owned or controlled by persons who are citizens of the United States or of one of its possessions.

Section 101 of the Federal Aviation Act

In *Northwest* and other cases the Department has taken the position that even if the participation of foreign interests in a U.S. carrier conforms to the specific requirements of the definition, still DOT may find that the carreier is not a citizen of the United States if foreign interests would have the power of exercise actual control over the airline through the ownership of nonvoting stock, or through other relationships. So far we are aware, DOT's assertion of authority to go beyond the specific requirements of the definition has been been affirmed by a court. It is not clear that a court would sustain DOT's interpretation of the Act.

Approach Followed by H.R. 3443

The legislation reported by the Committee, H.R. 3443, ehances DOT's ability to deal with leveraged buyouts and foreign ownership and control by establishing prior approval procedures and by clarifying the standards which the Department should use in reviewing acquisition.

Under the legislation, proposals to acquire 15% or more of the voting securities of a major airline would have to be filed with the Department of Transportation 30 days before they are implemented. The Department can extend this date if it needs more information. This procedure gives the Department the opportunity to disapprove a transaction before it is consummated.

The prior review timetable and procedures in H.R. 3443 are modeled on those of the Hart-Scott-Rodino Act which is used for antitrust review. These procedures have worked effectively in the antitrust area without burdening legitimate acquisitions and mergers. The procedures should work equally well in the airline field. Indeed, in most of the cases in which H.R. 3443 would require an acquiring party to give prior notification to DOT, the party would be required to give prior notification to the Department of Justice under Hart-Scott-Rodino at the same time. In many cases, review under Hart-Scott-Rodino would prevent a transaction from being completed during the same period of time as would H.R. 3443.

H.R. 3443 also establishes standards for DOT to use in reviewing acquisitions. The Department is directed to disapprove an acquisition if it would weaken a carrier financially so as to substantially impair its ability to operate safety or its competitive effectiveness, or require the carrier to dispose of a substantial portion of its aviation-related assets. Another ground for disapproval is that the acquisition would lead to a major reduction in the size of a carrier, if DOT is unable to find that there are any overriding public benefits from the reduction in size. Disapproval is also required if the acquisition would give a person who is not a citizen of the United States the power to exercise control over the airline.

H.R. 3443 is a moderate and reasonable approach to problems which threaten the future of our airline system. The only acquisition which would be disapproved are those which would seriously weaken an air carrier and impair its ability to provide safe, effective and reliable service. The bill will allow acquisitions and mergers which would benefit the public to go forward, while stopping

acquisitions which are based primarily on the desire for quick profits and threaten the future of a major airline.

SECTION-BY-SECTION ANALYSIS

The bill adds a new Section 420 to the Federal Aviation Act to provide for review by the Department of Transportation of acquisitions of the voting securities of major air carriers.

(A) GENERAL RULE

The acquisitions which are covered by the bill are acquisitions of 15 percent or more of the voting securities of a major air carrier or, in a case in which the acquiring party holds less than 15 percent of the voting securities, an acquisition which would put the acquiring party over the 15 percent line.

(B) WAITING PERIOD

If an acquisition is covered by the bill, the acquiring party may not acquire the stock until the Department of Transportation has been given notification, a 30-day waiting period has expired, and the Secretary has not disapproved the acquisition. The Secretary may allow an acquisition to go forward before the expiration of the 30-day waiting period.

(C) DISAPPROVAL

The bill establishes several standards for disapproval of an acquisition. First, an acquisition shall be disapproved if it is likely to weaken the acquired air carrier financially to such an extent that one of several consequences would occur. The acquisition must be disapproved if the carrier's weakened financial condition would cause a deterioriation in the carrier's ability to comply with established safety procedures, or would prevent the carrier from taking the steps necessary to continue to operate with the highest degree of safety, or if the financial weakening would force the carrier to dispose of a substantial portion of its aviation related assets in order to meet its financial obligations, or if the weakening would result in a substantial deterioration in the carrier's ability to compete in providing air transportation.

In making the foregoing determinations the Secretary shall give consideration to the ability of the acquired carrier to withstand a general economic recession. The Secretary shall consider the financial condition of the acquired carrier independently, without regard to the financial condition of other carriers which are not involved in an acquisition proposal. In making the determinations required by this paragraph, the Secretary shall consider, among other factors, whether there would be a substantial deterioration in the air carrier's ability to meet contractual commitments to build or expand airport or maintenance facilities or to hire and train qualified airmen, and whether such deterioration would result in any of the consequences which are grounds for disapproval under H.R. 3443.

A second ground for disapproval is if DOT finds that the probable intent of the acquiring party is to make a major reduction in the size of the air carrier by disposing of aviation related assets,

unless such disposition would have been, necessary in the absence of the acquisition, to avoid financial failure of the carrier, or unless the assets to be disposed of could not be used profitably by the carrier, or unless the disposition of assets would be in the public interest. In exercising his authority under this provision, the Secretary should not disapprove a transaction merely because it would result in a smaller carrier. It may sometimes be in the public interest to downsize an airline. The reported bill gives the Secretary discretion to approve acquisitions which would result in smaller carriers if the Secretary finds that there would be public benefits from the downsizing.

A third ground for disapproval is that the acquisition would result in a person who is not a citizen of the United States having power to exercise control over the air carrier.

This provision incorporates into the process mandated by this legislation the requirement already in Federal statute (Section 101 of the Federal Aviation Act) that the Secretary assures that at all times any U.S. carrier is under the effective control of U.S. citizens. The Secretary has had and would continue to have broad latitude in determining what would constitute effective foreign control of a U.S. carrier. Given that necessarily broad latitude, it is particularly important that the Secretary exercise this authority in a manner that is consistent, fair, and equitable to all parties, specifically by assuring that the same standards are applied to all airlines to the extent that the relevant facts with regard to each aspect of each case are similar to those in any other case. For example, in the consent Order discussed above, the Secretary found that there would be effective foreign control of Northwest, in view of the power to exercise control arising from such situations as a foreign airline sitting on the board of a U.S. carrier, a foreign airline providing more than 25 percent of the equity investment in a U.S. carrier, and a foreign airline having the right to establish an advisory committee.

The Committee believes that it is imperative that the Secretary makes determinations of this type in a manner which is consistent and nondiscriminatory among all U.S. carriers, not only to ensure fairness to the airlines involved, but also to avoid the competitive distortions which would result from unequal regulatory treatment, to protect the public interest in keeping all U.S. carriers under the control of U.S. citizens, and to preserve the Secretary's authority from challenges that it is being exercised in an arbitrary way. Thus we would expect any finding of effective foreign control with regard to any aspect of one carrier's circumstances to be applied similarly to any other carrier with regard to the same aspect of its circumstances. Government rules, policies, and precedents should be consistently applied without regard to carrier identity.

A fourth ground for disapproval is that the acquiring person is not providing in a timely manner, information required by the Secretary. This provision is designed to prevent the acquiring person from avoiding DOT disapproval by withholding necessary information until the 30-day waiting period has elapsed.

(D) FORM OF NOTIFICATION AND OTHER RULES

The bill gives the Secretary authority to establish rules for the submission of necessary information by the acquiring party and by the air carrier. Not later than ten days after the date of enactment, the Secretary shall issue the regulations necessary to carry out the objectives of the Section.

(E) EXTENSION OF WAITING PERIOD

If additional information is requested, the 30-day waiting period may be extended until 20 days after the Secretary receives supplemental information from the acquiring party or, in the case of an air carrier, 20 days from the date the extra information is due.

(F) PROTECTION OF INFORMATION

The bill further provides that information filed with the Secretary shall be exempt from public disclosure under the Freedom of Information Act, but that nothing in the Section is intended to prevent disclosure to Congress or any duly authorized Congressional Committee.

(G) COMPUTATION OF VOTING SECURITIES

For purposes of determining the percentage of voting securities held by a person, the bill directs DOT to aggregate securities held by a person and any affiliates of the person.

(H) DEFINITIONS

"Major air carrier" is defined as an air carrier with annual revenues of more than $750,000,000.

"Voting Securities" is defined as any security which at present or upon conversion entitles the owner to vote for the election of directors of the issuer or, with respect to unincorporated issuers, persons exercising similar functions.

COMMITTEE ACTION AND VOTE

With respect to clause 2(l)(2)(A) and (B) of rule XI the Rules of the House of Representatives, the Committee, with a majority present favorably reported H.R. 3443 by a 23–5 division on October 18, 1989.

Prior to the Committee's action, the Subcommittee on Aviation held three days of hearings on the subject matter of the legislation on October 3, 4 and 16. On October 16, the Subcommittee on Aviation favorably reported H.R. 3443 to the Committee by Voice Vote.

OVERSIGHT FINDINGS AND RECOMMENDATIONS

With respect to clause 2(l)(3)(A) of rule XI of the Rules of the House of Representatives, the Committee reports that no separate hearings were held on the subject matter of the legislation by the Subcommittee on Investigations and Oversight.

With respect to clause 2(l)(3)(D) of rule XI of the Rules of the House of Representatives, the Committee has not received a report

from the Committee on Government Operations pertaining to the subject matter.

Congressional Budget Act Requirements

With respect to clause 2(l)(3)(B) of rule XI of the Rules of the House of Representatives, and in compliance with section 308(a) of the Congressional Budget Act of 1974 H.R. 3443 does not provide any new budget authority or new or increased tax expenditures.

With respect to clause 2(l)(3)(C) of rule XI of the Rules of the House of Representatives, the Committee has received the following report from the Congressional Budget Office under section 403 of the Congressional Budget Act of 1974.

U.S. Congress,
Congressional Budget Office,
Washington, DC, October 19, 1989.

Hon. Glenn M. Anderson,
Chairman, Committee on Public Works and Transportation,
U.S. House of Representatives, Washington, DC.

Dear Mr. Chairman: The Congressional Budget Office has reviwed H.R. 3443, a bill to amend the Federal Aviation Act of 1958 to provide for review of certain acquisitions of voting securities of air carriers, and for other purposes, as ordered reported by the House Committee on Public Works and Transportation, October 18, 1989. CBO estimates that enactment of the bill would result in costs to the federal government of $250,000 to $500,000 annually, assuming appropriation of the necessary funds.

H.R. 3443 would require that the Secretary of Transportation review certain acquisitions of voting securities of major air carriers. The bill specifies a number of factors that must be considered in determining whether or not a particular acquisition should be disapproved. CBO estimates that the additional workload created by H.R. 3443 would typically result in costs to the federal government of $250,000 to $500,000 annually. However, costs could be higher in some years if the number, size or complexity of any acquisitions is unusually great.

No cost would be incurred by state or local governments as a result of enactment of this bill.

If you wish further details on this estimate, we will be pleased to provide them. The CBO staff contact is Mitchell Rosenfeld, who can be reached at 226-2860.

Sincerely,

Robert D. Reischauer,
Director.

Inflationary Impact Analysis

With respect to clause 2(1)(4) of rule XI of the Rules of the House of Representatives, the Committee reports that there should be no inflationary impact on prices and costs in the operation of the national economy by enactment of H.R. 3443.

COST ESTIMATE OF LEGISLATION

With respect to clause 7(A)(1) of rule XIII of the Rules of the House of Representatives, the Committee report that H.R. 3443 authorizes no funding and that there should be no costs incurred by enactment of the bill other than the annual $250,000–$500,000 estimated by the Congressional Budget Office in its report to the Committee on the legislation.

With respect to clause 7(A)(2) of rule XIII of the Rules of the House of Representatives, the Committee reports that no cost estimate of H.R. 3443 was submitted to the Committee by the government agency.

CHANGES IN EXISTING LAW MADE BY THE BILL, AS REPORTED

In compliance with clause 3 of Rule XIII of the Rules of the House of Representatives, changes in existing law made by the bill, as reported, are shown as follows (existing law proposed to be omitted is enclosed in black brackets, new matter is printed in italic, existing law in which no change is proposed is shown in roman):

TITLE IV OF THE FEDERAL AVIATION ACT OF 1958

TITLE VI—AIR CARRIER ECONOMIC REGULATIONS

Sec. 401. Certificate of public convenience and necessity.

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Sec. 420. Review of certain acquisitions of voting securities of air carriers.

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TITLE IV—AIR CARRIER ECONOMIC REGULATION

CERTIFICATE OF PUBLIC CONVENIENCE AND NECESSITY

CERTIFICATE REQUIRED

SEC. 401. (a) * * *

* * * * * * *

SEC. 420. REVIEW OF CERTAIN ACQUISITIONS OF VOTING SECURITIES OF AIR CARRIERS.

(a) GENERAL RULE.—No person shall acquire, directly or indirectly, any voting securities of a major air carrier or person who controls a major air carrier unless the acquiring person files notification pursuant to the rules under subsection (d), the waiting period described in subsection (b)(1) has expired, and the Secretary has not disapproved such acquisition under subsection (c)—

(1) if such acquisition is of 15 percent or more of the voting securities of the acquired person; or

(2) if, before such acquisition, the acquiring person holds less than 15 percent of the voting securities of the acquired person and, as a result of such acquisition, the acquiring person would hold 15 percent or more of the voting securities of the acquired person.

(b) WAITING PERIOD.—

(1) GENERAL RULE.—The waiting period required under subsection (a) shall—

(A) begin on the date of receipt by the Secretary of the completed notification required under this section from the acquiring person; and

(B) end on the 30th day after the date of such receipt or such later date as may be set under subsection (e)(2).

(2) TERMINATION.—The Secretary may, in individual cases, terminate the waiting period specified in paragraph (1) and allow any person to proceed with any acquisition subject to this section and promptly shall cause to be published in the Federal Register a notice that the Secretary does not intend to take any action within such period with respect to such acquisition.

(c) DISAPPROVAL.—The Secretary shall dispprove an acquisition of voting securities subject to this section if the Secretary finds—

(1) that the acquisition is likely to weaken the acquired person financially to such an extent—

(A) that a deterioration in the ability of the air carrier to comply with its established safety procedures would occur;

(B) that the air carrier would be unable to take the steps necessary to continue to operate with the highest degree of safety;

(C) that the air carrier would be required to dispose of a substantial portion of its aviation-related assets in order to meet its financial obligations; or

(D) that a substantial deterioration in the air carrier's ability to compete in providing air transportation would result;

(2) that the probable intent of the acquiring person is to make a major reduction in the size of the air carrier by disposing of aviation-related assets; except in any case in which—

(A) such disposition would be necessary, in the absence of the acquisition, to avoid the financial failure of the air carrier,

(B) the assets to be disposed of could not be used profitably by the air carrier, or

(C) such disposition would be in the public interest;

(3) that the acquisition would result in a person who is not a citizen of the United States having power to exercise control over the air carrier; or

(4) that the acquiring person is not providing, in a timely manner, the documentary material and information required by the Secretary to make a decision regarding the acquisition under this section.

(d) FORM OF NOTIFICATION AND OTHER RULES.—

(1) IN GENERAL.—The Secretary, by regulation—

(A) shall require that the notification under subsection (a) be in such form and contain such information and documentary material relevant to a proposed acquisition as is necessary to enable the Secretary to determine whether such acquisition should be disapproved under this section, and

(B) may pescribe such other rules as may be necessary and appropriate to carry out the purposes of this section, including rules relating to the submission by the air carrier of information or documentary material described in subparagraph (A).

(2) DEADLINE FOR ISSUANCE OF REGULATIONS.—Not later than 10 days after the date of the enactment of this section, the Secretary shall issue regulations necessary to carry out the objectives of this section.

(e) EXTENSION OF WAITING PERIOD.—

(1) SUBMISSION OF ADDITIONAL INFORMATION.—The Secretary may, before the expiration of the 30-day waiting period specified in subsection (b)(1), require the submission of additional information or documentary material relevant to the proposed acquisition, from a person required to file notification with respect to such acquisition under subsection (a), from the air carrier, or from any officer, director, partner, agent, or employee of such person.

(2) DURATION.—The Secretary, in his discretion, may extend the 30-day waiting period specified in subsection (b)(1) for an additional period of not more than 20 days after the later of—

(A) the date on which the Secretary receives from the acquiring person or any officer, director, partner, agent, or employee of such person all of the information and documentary material required to be submitted pursuant to a request under paragraph (1); or

(B) the date by which the air carrier or any officer, director, partner, agent, or employee of the air carrier is directed to submit information or documentary material pursuant to a request under paragraph (1).

(f) PROTECTION OF INFORMATION.—Any information or documentary material filed with the Secretary pursuant to this section shall be exempt from disclosure under section 552 of title, 5, United States Code, and no such information or documentary material may be made public, except as may be relevant to any administrative or judicial action or proceeding. Nothing in this section is intended to prevent disclosure to either House of Congress or to any duly authorized committee or subcommittee of Congress.

(g) COMPUTATION OF VOTING SECURITIES.—For purposes of this section, the amount or percentage of voting securities of a person which are acquired or held by another person shall be determined by aggregating the amount or percentage of such voting securities held or acquired by such other person and each affiliate thereof.

(h) DEFINITIONS.—As used in this section—

(1) MAJOR AIR CARRIER.—The term "major air carrier" means an air carrier with annual revenues of more than $750,000,000.

(2) VOTING SECURITIES.—The term "voting securities" means securities which at present or upon conversion entitle the owner or holder thereof to vote for the election of directors of the issuer or, with respect to unincorporated issuers, persons exercising similar functions.

DISSENTING VIEWS OF HON. ARLAN STANGELAND

With great reluctance, I must oppose H.R. 3443 in its current form. The bill thrusts the Secretary of Transportation into the inappropriate role of second-guessing business decisions, sends the wrong signal to the marketplace, and gets us closer to re-regulating the airline industry.

I appreciate the hard work and sincere efforts of my colleagues. The Committee leadership is responding to a growing concern about leveraged buyouts and their potentially adverse impact on safety and industry competition. I have no problem with their intent to ensure airline safety. That is one of this Committee's fundamental purposes and obligations to the public. However, I do have a problem with legislating in areas that in my view are best left to the private sector.

As recently stated by the Secretary of Transportation, H.R. 3443 would send the wrong message to the investment community, carriers, foreign governments, and the public. In many ways, our bill signals a retreat from deregulation, which has benefited consumers significantly over the years. Current law already provides the Secretary with authority to review safety, competition, financial fitness and citizenship requirements.

I also have concerns about some of the bases for the Secretary to veto proposed acquisitions. We may be straying too far from our traditional areas of concern when we address the sale of aviation-related assets. Like the Administration, I believe we should as a general rule encourage the free flow of capital among countries and allow marketplace dynamics to determine the financial structure of airlines.

While opposing the bill, I do recognize some legitimate safety concerns may be involved in selected transactions. As H.R. 3443 moves through the legislative process, I will work with my colleagues to increase the Secretary's flexibility and provide a better balance between intervention into the marketplace and continued passenger safety.

ARLAN STANGELAND.

DISSENTING VIEWS

We oppose H.R. 3443, legislation which will stop all airline acquisitions—whether leveraged buyouts (LBOs), straight cash purchases, or any other kind—good and bad alike. The mandatory 30-day freeze on every kind, size, and shape of acquisition of airline share will kill many otherwise viable market transactions without any proven justification. Worst of all, the Department of Transportation—not previously known for its expertise in capital markets or corporate finance—will now sit in judgment in place of the market to determine when, whether and to whom American shareholders can buy or sell their shares.

While we share the Committee's stated objectives of promoting competition within the airline industry, obtaining premium safety for air travelers, and enforcing existing laws concerning foreign ownership, the proposed legislation would, in fact, have the contrary, adverse effect of hurting both the airline industry and the travelling public by reducing the attractiveness of new investment in air carriers and limiting competition within the industry.

There are several trenchant flaws in the bill.

First: it is absolutely unnecessary to stop every open market transaction in airline shares dead in its tracks, simply because 15% ownership is involved. There is much ballyhoo in behalf of the bill about leveraged buyouts, but the bill makes not the slightest effort to address itself to these particular kinds of transactions. Rather, every transaction in shares of an airline is treated in the same fashion. This is a blatant example of throwing out the baby with the bath water—unless one believes that every free market sale of control is presumptively bad.

Second: even if it were thought desirable to give the Secretary of Transportation an advance opportunity to review sale-of-control transactions to determine their compliance with existing laws concerning foreign ownership and safety, the present bill goes well beyond that objective. Far less intrusive would be granting the Secretary "stop order" authority, in parallel with that already possessed by the Securities and Exchange Commission—thus permitting unobjectionable transactions to proceed unimpeded. The effect of a mandatory 30-day freeze in all cases (which may be extended to 50 days by the Secretary of Transportation) will be to jeopardize the ability of acquirors to obtain fixed-rate financing commitments from normal commercial sources, or alternatively to drive commitment fees much higher. Given the routine fluctuation of share prices in the marketplace, requiring that a firm-price purchase commitment be held open from 30 to 50 days additional will, in practical effect, kill many otherwise viable transactions.

Third: the bill contains an unsupportable presumption against airline divestiture of assets. The airline industry is increasingly concentrated, and costs of entry to the market are high. In most

cases, redeployment of existing airline assets will be one of the most attractive ways of starting a new airline. Yet the current legislation would hold up even a financially sound acquisition of airline shares in the marketplace, if the purpose of the acquisition is to spin off substantial airline assets. Such a transaction would be treated as if it were an LBO, even if it is not; only an affirmative finding by the Secretary of Transportation that the proposed sale of assets is in the "public interest" could permit the transaction to proceed, and then only after the expiration of the mandatory 30-day freeze. This restriction is strongly biased toward bigness, and toward the vertical integration of service and repair, catering, fueling, and other necessary functions. The Committee received no evidence to support this unsound economic presumption; to the contrary, it is likely that both the American consumer and the airline industry will be harmed by such anticompetitive restrictions.

Fourth: while allegedly designed to protect the safety of air carriers, the bill could in fact make American airlines more dangerous to fly. Safety and maintenance require substantial investment. By making airline shares less attractive to investors, this bill would raise the cost of capital in the industry, and necessarily limit the availability of needed new capital. Restricting the sale of airline shares in the free market, therefore, could hurt rather than protect the public by overriding the judgment of the marketplace as to an airline's best capital structure. In this regard, the Committee chose to ignore the emphatic testimony of the Dean of the Yale School of Management—the only witness to offer objective evidence on the point—that there is currently no ascertainable correlation between airline capital structures and their safety records.

Fifth: the bill, while styled as a neutral measure addressed to industry-wide problems, is in fact targeted at particular transactions. Widespread press coverage of the Committee's action has described the purpose of this legislation as stopping the proposed acquisitions of American and United Airlines. In fact, the Committee's action has already had this effect; in response to the bill, both offers have been withdrawn by the bidders. Such special-interest legislation should be eschewed by responsible legislators.

Sixth: As evidenced by recent events, this anti-investment bill can be expected to have a substantial, adverse impact on America's capital markets. On Friday, October 13, when the Dow Jones Industrial average fell more than 190 points in one day, press reports attributed much of the blame to this Committee's consideration of the present bill. Just as with the Brady Commission's conclusion that the crash of October 1987 was largely due to the Ways and Means Committee's announcement of pending anti-takeover legislation, so, too, this month's drop was precipitated by the massive sell-off of airline stocks that followed trading halts in United and American shares. Before Congress undertakes to pass such unduly restrictive measures affecting the nation's stock markets, it should at least hear testimony from corporate finance experts, the Securities and Exchange Commission, the Department of the Treasury, and the investment community. In fact, however, the only evidence presented in hearings on this bill came from congressional sponsors and anti-takeover labor union leaders.

These are just a few of the many concerns we have over this serious flawed legislation—and we are not alone in expressing them. The Bush Administration has sent a clear message stating its opposition to this bill. The Department of Transportation, in a letter to this Committee, stated clearly that "should this bill or any similar legislation be submitted to the President for his signature," the Secretary "would join the President's other senior advisors in recommending that he veto it." The Department further reaffirmed that sufficient authority exists under present law to ensure the safety, financial fitness and U.S. control of air carriers.

Passage of this bill would send exactly the wrong message to our capital markets at a time when we all profess to be seeking ways to increase U.S. savings, investment, and competitiveness by reducing the cost of capital. Presently, America leads the world in airline services; our lead should not be squandered. This legislation, while well intended, would do just that. It would cause even more broad damage in the stock market as a whole. It is seriously flawed, and should be defeated.

CHRIS COX.
RON PACKARD.
MEL HANCOCK.
TOM PETRI.
CASS BALLENGER.
DENNIS HASTERT.
LARRY E. CRAIG.
BOB MCEWEN.

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